With Smartphone Deals, Patents Become a New Asset Class
By STEVE LOHR

for The New York Times

TRADING IDEAS

Steven Steger, left, and David Berten, co-founders of Global IP Law Group, a firm specializing in patent legal and advisory work. It can be hard to keep up with the pace of change in the industry: “In patent law, you’re at the cutting edge of everything, and that’s shifting all the time,” Mr. Berten said.

David Berten has spent his legal career as a mercenary student of technological change. He has educated himself in one field after another: chemical coatings, genetics, navigation systems, semiconductors and digital communications software.

Keeping up is a constant challenge. This month, the 48-year-old lawyer was in his Chicago office, discussing past cases while scanning news Web sites and technology blogs for details on Apple’s iPhone 5, which was being introduced in San Francisco that day.

“We have to know what’s in it,” Mr. Berten said. “In patent law, you’re at the cutting edge of everything, and that’s shifting all the time.”

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His firm, the Global IP Law Group, is a sign of the fast-emerging patent marketplace. Global IP, founded in 2009, is one of several boutique firms specializing in patent legal and advisory work that have cropped up recently. Silicon Valley is home to a cluster of them, including Inflexion Point Strategy, Epicenter IP Group and 3LP Advisors.

Though created by lawyers, these companies are hybrids: more merchant banks than law firms. They have legal expertise, but focus on valuing and selling patents and giving strategic advice.

Global IP made its name as an adviser to Nortel Networks, a bankrupt Canadian telecommunications maker that sold its 6,000 patents for $4.5 billion to a group of six companies led by Apple.

The high price paid for the Nortel portfolio set off a bull market in patents that can claim some snippet of smartphone technology. By one estimate, as many as 250,000 patents may touch a modern smartphone. So patents have become defensive and offensive weapons in the smartphone wars, with the major companies suing one another in courtrooms around the world.

A few months after the sale, the big loser in the Nortel auction made its move. Google agreed to buy Motorola Mobility for $12.5 billion, and about $5.5 billion of that was the value of Motorola’s patents, Google said in a government filing this year. Smartphones made by Samsung and other companies are powered by Google’s Android software, making Google and Apple archrivals in smartphone technology.

The smartphone patent megadeals may be over now that the two main adversaries have armed themselves. An attempt by the bankrupt Eastman Kodak to sell 1,000 digital imaging patents stumbled recently, as bids from potential buyers like Apple and Google came in far below the $2.2 billion to $2.6 billion Kodak had said the patents were worth.

But the huge deals, while exceptional, were made possible by a broader trend: patents have become a new asset class.

Traditionally, patents sat on corporate shelves and were occasionally used as bargaining chips in cross-licensing deals with competitors. But that began to change in the 1990s, when technology companies like Texas Instruments and I.B.M. started to regard their patent portfolios as sources of revenue, licensing their intellectual property for fees.

Today, companies routinely buy and sell patents, mostly in deals that draw little attention, for millions of dollars instead of billions. The question, experts say, is how big the market will become.

“Patents are a tricky asset to trade,” said Josh Lerner, an economist at the Harvard Business School. “But there is clearly a huge amount of value in intellectual property. And I think what we’re seeing is the beginning of a lot more monetization and trading of intellectual property rights.”

A sizable specialist industry has developed to build the marketplace for trading ideas. The players include patent aggregators like Intellectual Ventures and RPX, patent brokers like Ocean Tomo and ICAP, hedge funds,
investment banks and law firms.

Yet boutique firms like Global IP play an important role, offering specialized expertise and an entrepreneurial approach. “We take patents and try to make money from them in all ways known to man — sales, licensing and litigating, if necessary,” Mr. Berten said.

Global IP opened in 2009 with two lawyers, Mr. Berten and Steven Steger. The firm now has 10 lawyers. About two-thirds of its business is selling patents, and it is working on more than two dozen portfolios. Most work is done on a contingency basis, with a sliding scale of fees that can reach 40 percent on projects that involve litigation, Mr. Steger said.

In the Nortel project, Mr. Berten and his team built a vast database of the Nortel patents, tracking the history of each through the government patent office, citations in other patent applications, uses in license agreements and filings in other countries. “It was a boatload of work,” said George Riedel, former chief strategy officer at Nortel.

Mr. Berten and Mr. Riedel, along with Nortel’s bankers from Lazard, made presentations to companies in Silicon Valley and Europe. Mr. Riedel said Mr. Berten showed an impressive grasp of detail, down to individual patents and claims, when challenged by lawyers at the major technology companies.

His job, Mr. Berten said, was to “identify the value of patents and then demonstrate that value to potential buyers.”

The auction was run by Nortel’s bankruptcy lawyers at Cleary Gottlieb Steen & Hamilton. The winning bid of $4.5 billion was well above the $2 billion to $3 billion projected. “Sure, I was surprised,” Mr. Riedel said. “We were fortunate to be in the midst of an ecosystem battle in smartphones.”

In the Kodak bankruptcy, Global IP was brought on in a very different role: as an outside adviser to the unsecured creditors, including Wal-Mart Stores and Sony Pictures Entertainment. Its job was to determine if the proposed auction was undervaluing the patents, and to advise the creditors if they might be better off taking another approach, like licensing the patents.

The very different experiences of Nortel and Kodak point to the many factors that go into pricing patents. Timing, competitive forces, regulation and court rulings all have an effect, said Ronald S. Laurie, managing director of Inflexion Point Strategy.

“Patents are a volatile, spot market,” he said. “This is a market, but a market that is more like art than stocks or oil.”

Ron Epstein, chief executive of Epicenter IP Group, agreed that pricing patents, especially large portfolios, was difficult. But he said he thought corporate trading in patents would become more commonplace, and pricing more routine. Someday, he predicted, patent acquisition costs may be a standard line item in corporate earnings statements.

“By fits and starts, we are moving to a more efficient marketplace for innovation,” Mr. Epstein said.

Calling patents an asset class is shortsighted, said Kevin Rivette, a founder of 3LP Advisors. The larger value of a portfolio, he said, can be as a strategic tool to negotiate lower costs from a supplier or to alter a rival’s product plans.
“You can use patents to change the competitive landscape,” he said.

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